

# AUDIT OF LEGAL FEES PAID TO BAKER & BOTTS

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Audit Report No. 99-022  
April 14, 1999



OFFICE OF AUDITS

OFFICE OF INSPECTOR GENERAL

**Material has been redacted from this document to protect personal privacy, confidential or privileged information.**

# FDIC

Federal Deposit Insurance Corporation  
Washington, D.C. 20434

Office of Audits  
Office of Inspector General

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April 14, 1999

**TO:** James T. Lantelme  
Assistant General Counsel  
Legal Operations Section  
Legal Division



**FROM:** David H. Loewenstein  
Assistant Inspector General

**SUBJECT:** *Audit of Legal Fees Paid to Baker & Botts*  
(Audit Report No. 99-022)

This report presents the results of an audit of fees paid to Baker & Botts, a law firm hired by the FDIC to provide legal services. The audit was conducted by the independent public accounting firm of Metcalf Rice Fricke & Davis. The objective of the audit was to determine whether the law firm's legal bills were: (1) adequately supported by source documentation, (2) prepared in accordance with applicable agreements, and (3) representative of the cost of services and litigation that had been approved in advance by the Legal Division. The audit covered all payments to Baker & Botts from July 1, 1997 through June 30, 1998 which included 18 fee bills totaling \$2,277,457.

The Legal Division issued a written response received April 5, 1999 (see Appendix II) to a draft of this report that provided the requisites for a management decision on each of the recommendations. In its response the Legal Division disallowed questioned costs totaling \$6,564. The OIG's evaluation of management's comments is presented in Appendix I.

If you have any questions, please call me at (202) 416-2412 or Allan H. Sherman, Deputy Assistant Inspector General, at (202) 416-2522.

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INDEPENDENT ACCOUNTANTS' REPORT  
ON APPLYING AGREED-UPON PROCEDURES

Office of the Inspector General  
Federal Deposit Insurance Corporation:

We have performed the procedures (Procedures) enumerated in the Appendix, which were agreed to by the Office of the Inspector General (OIG), Federal Deposit Insurance Corporation (FDIC), solely to assist OIG in determining whether the fee bills submitted by Baker & Botts, L.L.P. (Firm) and paid by the FDIC from July 1, 1997 through June 30, 1998, were adequately supported, consistent with the terms and conditions of the governing agreements and were representative of the cost of services and litigation which was approved in advance. This agreed-upon procedures engagement was performed in accordance with standards established by the American Institute of Certified Public Accountants and with applicable Government Auditing Standards. The sufficiency of these Procedures is solely the responsibility of the specified users of the report.

Consequently, we make no representations regarding the sufficiency of the Procedures described in the Appendix either for the purpose for which this report has been requested or for any other purpose.

The Procedures and Findings of this engagement are included in the accompanying pages 2 through 6 of this report.

We were not engaged to, and did not, perform an examination, with the objective of expressing an opinion on whether the fee bills present fairly the expenses and activities of the cases for which they were submitted. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

This report is intended solely for the use of OIG and FDIC, and should not be used by those who have not agreed to the Procedures and taken responsibility for the sufficiency of the Procedures for their purposes.

*Metcalf Rice Fricke & Davis*

September 23, 1998  
Atlanta, Georgia

BAKER & BOTTS, L.L.P.  
WASHINGTON, D.C.

**BACKGROUND**

The FDIC incurs legal fees when attorneys and law Firms are retained to assist the FDIC in litigation and other legal services. The authority and responsibility for the retention of outside counsel, oversight of services rendered, and approval of fee bills resides with the General Counsel and the Legal Division. The OIG performs audits of fee bills, similar to other contract audits, to ensure that such claims are adequately supported and comply with cost limitations set forth by the FDIC.

**OBJECTIVE, SCOPE AND METHODOLOGY**

The objective of the engagement was to determine whether the fee bills submitted by the law firm were: (1) adequately supported by source documentation, (2) prepared in accordance with the applicable agreements, and (3) representative of the cost of services and litigation which was approved in advance by the Legal Division. The engagement scope covered all FDIC payments to Baker & Botts, L.L.P. (the Firm) from July 1, 1997 through June 30, 1998, which included 18 fee bills totaling \$2,277,457.

Fieldwork included interviews and tests of transactions in the law offices of Baker & Botts, L.L.P. in Washington, D.C. The engagement was conducted in accordance with standards established by the American Institute of Certified Public Accountants and with applicable *Government Auditing Standards* and, thus, included such tests of the accounting records and other procedures as we considered necessary under the circumstances. We obtained an understanding of the internal control structure related to the Firm's billing process. With respect to the internal control structure, we obtained an understanding of the design of the Firm's billing policies and procedures and whether they have been placed in operation. We assessed control risk in order to determine our Procedures and for the purpose of evaluating the fees and expenses billed to the FDIC and not to provide an opinion on the internal control structure. Accordingly, we do not express such an opinion.

The fee bills were tested for adequacy of source documentation, compliance with the cost provisions of the agreements in effect, and the appropriateness of the charges. The fee bills were tested for compliance with the FDIC 's policies and procedures for submitting fee bills as included in the *Guide for Outside Counsel* (Guide) and the Legal Services Agreements (LSA's) in effect between the FDIC and the Firm.

In order to identify billed amounts disallowed by the Legal Division prior to our engagement, we compared the amounts billed by Baker & Botts, L.L.P. to the amounts paid by the FDIC. We have adjusted the questioned costs in our report for costs previously disallowed to preclude duplication.

The Procedures tested covered relevant source documents supporting legal fee bills. The sampled fee bills were reviewed in terms of two major components: fees for professional services (charges based on hourly rates) and claims for reimbursable expenses such as travel, courier services and document reproduction. An exit conference was held with Baker & Botts, L.L.P. representatives to discuss the preliminary conditions at the end of fieldwork.

### SUMMARY OF SIGNIFICANT FINDINGS

We concluded that except for \$8,434 in fees and expenses detailed in the Findings and Recommendations section of this report, billings submitted by Baker & Botts, L.L.P. and paid by the FDIC from July 1, 1997, through June 30, 1998, were supported by source documentation, prepared in accordance with applicable agreements, and were representative of the cost of services and litigation which was approved in advance by the Legal Division. The audit identified questioned costs related to fees paid for professional services in the amount of \$4,010. These services include fees for an attorney not authorized under the LSA and non-reimbursable administrative charges. In addition, we are questioning expenses in the amount of \$4,424. The expenses consist of charges for airfare, lodging and per diem in excess of FDIC approved rates and local meal charges. The questioned costs are summarized in the following table.

<b>Summary of Questioned Costs</b>		
	<b>Recommendation</b>	<b>Questioned</b>
<b>Description</b>	<b>Number</b>	<b>Costs</b>
Unauthorized Attorney	1	\$ 1,870
Non-Reimbursable Administrative Charges	2	\$ 2,140
<b>Subtotal Fees</b>		<b>\$ 4,010</b>
Excess Travel Charges	3	\$ 3,794
Local Meals Charges	4	\$ 630
<b>Subtotal Expenses</b>		<b>\$ 4,424</b>
<b>Total Fees and Expenses</b>		<b>\$ 8,434</b>

### FINDINGS AND RECOMMENDATIONS

#### **Unauthorized Attorney**

The Firm billed the FDIC \$1,870 for 5.5 hours at a rate of \$340 for an attorney not approved on the LSA or amendments. The Guide requires written authorization to add additional personnel to the LSA. Our review of 100% of the attorneys' billing time disclosed that all other attorneys had been approved by the FDIC and that they were billed at approved rates.

**Recommendation 1:** The Assistant General Counsel, Legal Operations Section, should disallow \$1,870 for an unauthorized attorney.

### **Non-Reimbursable Administrative Charges**

The Firm billed the FDIC \$2,140 for Non-Reimbursable Administrative Charges. Tasks billed included copying, faxing, invoice preparation, shipping and packing. The Guide prohibits charges for administrative tasks which are considered as overhead. The Firm agreed during a meeting on October 9, 1998 that these billings were in error and should not have been charged to the FDIC.

**Recommendation 2:** The Assistant General Counsel, Legal Operations Section, should disallow \$2,140 for Non-Reimbursable Administrative Charges.

### **Excess Travel Charges**

The Firm billed the FDIC \$4,949 for business class airfare to London, England on invoice numbers 455276 and 459249 when the highest coach airfare was \$1,504. The Guide states that “the FDIC will only pay airfare up to the highest coach fare,” therefore, we question costs of \$3,445 for excess airfare. The Firm also billed the FDIC ~ in travel costs which exceeded the maximum per diem rates established by the FDIC.

**Recommendation 3:** The Assistant General Counsel, Legal Operations Section, should disallow \$3,794 for excess travel charges.

### **Local Meals Charges**

The Firm billed the FDIC \$630 for meal costs related to lunches while working in their Washington, D.C. office. The Guide does not permit charges for meals except during out of town travel.

**Recommendation 4:** The Assistant General Counsel, Legal Operations Section, should disallow \$630 for local meals charges.

BAKER & BOTTS, L.L.P.  
WASHINGTON, D.C.

**PROCEDURES**

**General**

1. Obtained a listing of the population of legal fee invoices to be reviewed for FDIC payments from July 1, 1997 through June 30, 1998.
2. Obtained and reviewed copies of the FDIC Legal Services Agreements (LSA) in effect for the period July 1, 1997 through June 30, 1998, as well as the Firm's responses to the FDIC's law Firm questionnaire.
3. Requested a summary of the Firm's usage of the FDIC Legal Research Bank, including the matters referenced.
4. Obtained annotated copies of legal fee invoices from the Firm, showing exceptions taken to Firm's bills by case managing attorneys and fee bill review technicians.
5. Obtained a completed management representation letter from the Firm.

**Fitness and Integrity**

6. Determined whether the Firm requested and/or received any conditional waiver of a conflict of interest from the FDIC Legal Division.
7. Reviewed the Firm's malpractice insurance policy to determine the extent and duration of the Firm's coverage.

**Quantitative Review of Legal Fee Bills**

8. Performed quantitative test work and validated the mathematical accuracy of all 18 sampled invoices (the Sample).
9. Compared the names and billing rates used on all sampled invoices with the names and rates indicated on the LSA.
10. Selected a sample of attorneys who had devoted substantial time to FDIC related matters and interviewed them to obtain adequate explanation for hours worked each day when hours charged exceeded twelve hours.
11. Reviewed time sheets of the sampled attorneys for mathematical accuracy and scheduled total hours on a daily basis for one billing month. Reviewed schedules for reasonableness and obtained explanations for unusual entries.
12. Determined the Firm's standard billing rates and compared them to the rates billed on the invoices in the Sample.
13. Reviewed time sheets for a portion of the sampled invoices to determine if there had been any inefficiency indicated by excessive rotation between projects.

BAKER & BOTTS, L.L.P.  
WASHINGTON, D.C.

**PROCEDURES**

14. Reviewed time sheets for a portion of the sampled invoices to determine if there had been excessive research time, and to determine if the Firm had used the FDIC's Legal Research Bank.
15. Reviewed a portion of the sampled invoices for extent of use of paralegals and summer help.
16. Reviewed time sheets and a portion of the sampled invoices to determine the Firm's billing policy on time spent for:
  - preparation of invoices,
  - traveling,
  - researching the Firm's own conflicts of interest, and
  - preparation of plans, budgets and status reports.
17. Reviewed a sample of deposition transcripts for:
  - amount of time spent and charged by the court reporters and the attorneys, and
  - unauthorized attorneys who attended the depositions.

**Analysis of Expenses Charged**

18. Performed an analysis of expenses charged; validated the mathematical accuracy of all invoices in the Sample and determined the percentage of the total expenses charged for each expense category.
19. Compared amounts billed for expenses charged to amounts paid by the Firm to outside contractors to determine if billing had occurred at cost for the following categories:
  - document reproduction charges,
  - outside database services,
  - deposition transcripts, hearing transcripts, court fees and filing fees, and
  - expert witness and consultant fees.
20. Evaluated the adequacy of supporting documentation for document reproduction charges, as well as the reasonableness of the quantities billed.
21. verified that expenses billed were related to FDIC matters.
22. Examined expense charges to determine whether charges for outside database services were:
  - in compliance with the LSA and the Guide,
  - related to the applicable FDIC matters, and
  - adequately documented.
23. Reviewed payments received from the FDIC to determine whether any duplicate payments had been received by the Firm.
24. Reviewed billing periods on invoices to determine whether the Firm had double-billed FDIC for overlapping billing periods.

## **MANAGEMENT COMMENTS AND OIG EVALUATION**

On April 5, 1999, the General Counsel provided a written response to the draft report. The response is presented in Appendix II to this report.

The General Counsel disallowed the recommended questioned costs for recommendations 2, 3 and 4 totaling \$6,564. The Legal Division ratified \$1,870 of the recommended questioned costs for recommendation 1 based on additional information provided by the law firm after issuance of the draft report.

In recommendation 1, the OIG recommended disallowance of \$1,870 for legal fees billed for unauthorized personnel. The questioned costs related to fees billed for an attorney who was not listed on the legal services agreement between FDIC and the firm. The Legal Division ratified these charges based on a letter provided by the firm that indicated that the FDIC supervising attorney was aware of the work of the attorney and that the rate billed for the attorney was commensurate with approved LSA rates.

Appendix III presents management's proposed action on our recommendations and shows that there is a management decision for each recommendation in this report. After considering additional information provided by the firm and management's response to the draft report, we will report questioned costs of \$6,564 in our *Semiannual Report to the Congress*.

**FDIC**

Federal Deposit Insurance Corporation

Washington, D.C. 20429

Legal Division

April 2, 1999

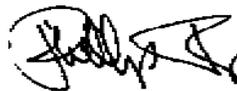
MEMORANDUM TO: David H. Loewenstein  
Assistant Inspector General



THROUGH: William F. Kroener, III  
General Counsel



William S. Jones  
Supervisory Counsel



FROM: Phillip F. Ty  
Counsel

SUBJECT: Audit of Legal Expenses Paid by FDIC to Baker & Botts  
(Washington, D.C.)

This memorandum constitutes the Legal Division's response to both the Office of Inspector General's draft audit report ("Report") (Exhibit A) and the response from Baker & Botts ("Firm") dated February 5, 1999 (Exhibit B). The audit was conducted by Metcalf Rice Fricke & Davis, an independent public accounting firm ("IPA"). The audit scope covered all FDIC payments to the Firm from July 1, 1997 through June 30, 1998, which included 18 fee bills totaling \$2,277,457. The Report questions \$8,434. After reviewing the Report and the Firm's response, the Legal Division will disallow a total amount of \$6,564.

The Legal Division's position regarding each recommendation is explained below in the order in which it appears in the Report.

**Recommendation No. 1: Disallow \$1,870 for an unauthorized attorney.**

The Report states that the Firm billed the FDIC \$1,870 for 5.5 hours at the rate of \$340 per hour for an attorney who was not approved on the Legal Services Agreement ("LSA") or amendments.

The Firm explains that the "unauthorized attorney" is [material redacted], who is the partner-in-charge of the Intellectual Property practice group in its Washington, D.C. office. The Firm states

that the entire amount of questioned cost is attributable to work that [material redacted] performed in connection with a request by the FDIC for assistance in drafting a licensing agreement. In connection with that project, the Firm states that [material redacted] supervised and directed the work of [material redacted], an associate in the Firm.

According to the Firm, the FDIC attorney who supervised the work, and dealt directly with [material redacted] on the matter, is [material redacted], an FDIC Counsel. When the auditors notified the Firm of this issue, the Firm explained the situation to [material redacted], and requested that she confirm that the involvement of [material redacted] in the project was approved by the FDIC. The Firm, in its response, attached a copy of its letter to [material redacted], on which she indicated her approval. Due to the FDIC supervising attorney's approval and because the partner's billed rate was commensurate with approved LSA rate discounts given by the Firm, the Legal Division will ratify the questioned charges.<sup>1</sup>

**The Legal Division accepts the Firm's explanation and will allow \$1,870.**

**Recommendation No. 2: Disallow \$2,140 for non-reimbursable administrative charges.**

According to the Report, the Firm billed the FDIC \$2,140 for non-reimbursable administrative charges. Tasks billed included copying, faxing, invoice preparation, shipping and packing, which are considered as overhead. The Firm agrees that those billings were in error, and should not have been charged to the FDIC.

**The Legal Division will disallow and demand reimbursement of \$2,140 for non-reimbursable administrative charges.**

**Recommendation No. 3: Disallow \$3,794 for excess travel charges.**

The Report states that the Firm billed the FDIC \$4,949 for business class airfare to London, England, when the highest coach airfare was \$1,504. The Guide for Outside Counsel ("Guide") states that the FDIC will only pay airfare up to the highest coach fare. Therefore, the Report questions costs of \$3,445 (\$4,949 less \$1,504) for excess airfare. The Report also states that the Firm billed the FDIC \$349 in travel costs which exceeded the maximum per diem rates established by the FDIC.

The Firm explains that with regard to the questioned cost of \$3,445 for excess airfare, the purpose of the trip was to take the deposition of a hostile witness. The witness refused to testify voluntarily, and it was necessary to seek the aid of the court to compel her testimony. The witness also claimed to be extremely busy, and unavailable except during limited hours on a few particular days. Shortly before the deposition was to occur, the court held a hearing on the issue,

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<sup>1</sup>Since the General Counsel has complete delegated authority regarding hiring and paying outside counsel with respect to issues raised by the Report, his signing of this memorandum should be deemed a ratification or approval of billing rates to the extent indicated herein.

and issued an order compelling attendance at the deposition on one of the days the witness had said she would be available. Because the hearing took place only a few days before the deposition, it was necessary to obtain a ticket quickly. The attorney involved did not check the cost difference between business class and coach class fares. The Firm acknowledges that the excess amount should not have been billed and it does not object to the questioned cost of \$3,445.

With respect to the other finding of \$349 in excess travel costs, the Firm explains that it appears that the questioned charges may have been attributable to instances where one attorney paid the total amount of a dinner bill for a group of attorneys, experts, and witnesses who were all in attendance at the same deposition or court proceeding. The Firm also states that it appears that, if the total meal charge had been divided into individual checks, none of the attorneys or witnesses would have exceeded the applicable per diem amounts. However, the Firm does not object that \$349 in travel costs be disallowed.

**The Legal Division will disallow and demand reimbursement of \$3,794 for excess travel charges.**

**Recommendation No. 4: Disallow \$630 in charges for local meals.**

According to the Report, the Firm billed the FDIC \$630 for meal costs related to lunches while working in their Washington, D.C. office. The Guide does not permit charges for meals except during out of town travel.

The Firm responds that it has reviewed the questioned charges and has determined that in every instance, the expense was not a charge for an individual attorney's meal, but was a charge for sandwiches for a working lunch meeting with attorneys, accountants, experts, and witnesses in connection with depositions in the [material redacted] case. The purpose of the meetings was to prepare the witness to testify before the deposition, or to discuss the deposition with the witness during the lunch break on the day of the deposition. In those instance, the Firm states that it had sandwiches delivered to its offices, and met with the witness in the conference room during the lunch break rather than going to a restaurant near the site of the deposition so that they could discuss the deposition testimony confidentially. The Firm also states that it has always been its understanding that the FDIC pays the cost of such working lunches. The Firm concludes that in light of the FDIC's past practice, it believes those charges are proper, however, because the questioned amount is small, it does not object to the disallowance of \$630 for local meals.

Ever since the publication of the FDIC *Guide for Outside Counsel* in December 1991, it has been the policy of the FDIC not to reimburse outside counsel for meal expenses unless they were incurred during travel. ("If business is conducted during a meal, appropriate time charges may be made at normal hourly rates, but charges for food, beverages and the like will not be reimbursed by the FDIC unless an attorney travels away from the home office overnight.") The *Outside Counsel Deskbook* published in June 1997 states that FDIC will not reimburse firms for "[m]eals outside of approved travel."

**The Legal Division will disallow and demand reimbursement of \$630 in charges for local meals.**

The Legal Division has determined that it will disallow and seek recovery of fees and expenses as follows (questioned costs are shown in parentheses):

1. Unauthorized Personnel	(\$1,870)	\$ -0-
2. Non-Reimbursable Administrative Charges	(\$2,140)	2,140
3. Excess Travel Charges	(\$3,794)	3,794
4. Local Meals Charges	(\$630)	<u>630</u>
Total:		\$6,564

The Assistant General Counsel is authorized to make such minor accounting corrections as may be required by the OIG but which do not affect the substantive position stated in this memorandum. The Legal Division expects to complete the collection process within 180 days from the issuance of the final audit Report by the OIG.

Attachments:

Tab A - OIG Draft Audit Report

Tab B - Firm's Response to the Draft Audit Report

### MANAGEMENT RESPONSES TO RECOMMENDATIONS

The Inspector General Act of 1978, as amended, requires the OIG to report the status of management decisions on its recommendations in its semiannual reports to the Congress. To consider FDIC's responses as management decisions in accordance with the act and related guidance, several conditions are necessary. First, the response must describe for each recommendation

- the specific corrective actions already taken, if applicable;
- corrective actions to be taken together with the expected completion dates for their implementation; and
- documentation that will confirm completion of corrective actions.

If any recommendation identifies specific monetary benefits, FDIC management must state the amount agreed or disagreed with and the reasons for any disagreement. In the case of questioned costs, the amount FDIC plans to disallow must be included in management's response.

If management does not agree that a recommendation should be implemented, it must describe why the recommendation is not considered valid. Second, the OIG must determine that management's descriptions of (1) the course of action already taken or proposed and (2) the documentation confirming completion of corrective actions are responsive to its recommendations.

This table presents the management responses that have been made on recommendations in our report and the status of management decisions. The information for management decisions is based on management's written response to our report.

<b>Rec. Number</b>	<b>Corrective Action: Taken or Planned/Status</b>	<b>Expected Completion Date</b>	<b>Documentation That Will Confirm Final Action</b>	<b>Monetary Benefits</b>	<b>Management Decision: Yes or No</b>
1	The Assistant General Counsel, Legal Operations Section, ratified \$1,870 for unauthorized personnel.	Completed	Legal Division Response	\$0	Yes
2	The Assistant General Counsel, Legal Operations Section, agreed to disallow \$2,140 for non-reimbursable Administrative Charges.	180 days from final report	Law Firm Refund Check	\$2,140 disallowed costs	Yes
3	The Assistant General Counsel, Legal Operations Section, agreed to disallow \$3,794 for Excess Travel Charges.	180 days from final report	Law Firm Refund Check	\$3,794 disallowed costs	Yes
4	The Assistant General Counsel, Legal Operations Section, agreed to disallow \$630 for local meals charges.	180 days from final report	Law Firm Refund Check	\$630 disallowed costs	Yes